

EXHIBIT A

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LOCAL TELECOMMUNICATIONS COMPETITIVE ENVIRONMENT:

OMAHA/COUNCIL BLUFFS MSA

1. Introduction

The competitive environment has changed significantly within Qwest's service territory of the Omaha, Nebraska MSA¹ over the past four years, with customers now enjoying the ability to choose between multiple providers of telecommunications services in that market. In 2000, for example, Qwest's primary local exchange competition was represented by CLECs, with a significant proportion of CLEC competition comprised by resale of Qwest's retail services. Cox, now Qwest's most significant competitor in the Omaha MSA, was offering telecommunication service at that time but did not offer service with the scope it has today. The local exchange market in 2004 has changed dramatically, with CLEC competition moving largely away from resold services and toward services provided via CLEC-owned facilities or via wholesale unbundled network

¹ The Omaha MSA encompasses the greater Omaha, Nebraska area as well as the Council Bluffs, Iowa area.

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elements (UNEs) purchased from Qwest. Additionally, intermodal competition now has a significant presence in the local exchange market in the form of wireless services and Voice over Internet Protocol (VoIP) telephony. While Qwest's local exchange access line base has declined by over [REDACTED] from December 2000 to February 2004,² CLEC lines and the number of wireless subscribers have increased very significantly, and VoIP is now a viable local service alternative for any customer with access to a broadband internet connection. The breadth of competitive alternatives in the Omaha MSA is now significant, and multiple competitors are now entrenched in that market. In this MSA, Qwest is no longer the dominant telecommunications provider.

2. Qwest's Local Exchange Base

As competitive local exchange alternatives have grown in the Omaha MSA, Qwest's local exchange access line base has rapidly eroded. Local exchange customers virtually throughout Qwest's service territory in the Omaha-Council Bluffs area now have the option of subscribing to local service from CLECs using either their own switches and network facilities or wholesale network elements purchased from Qwest. The following table summarizes the significant change in Qwest's residential and business retail access line base in the Omaha MSA³ from December 2000 to February 2004:

² This percentage does not account for new customers who subscribe immediately to the service of a CLEC without becoming a Qwest customer in the first instance.

³ Qwest service territory in the Omaha MSA includes the following Qwest wire centers in Nebraska: Bennington, Elkhorn-Waterloo, Gretna, Omaha 78th St., Omaha 84th St., Omaha 90th St., Omaha Bellevue, Omaha 135th St., Omaha Fort St., Omaha Fowler St., Omaha 156th St., Omaha Izard St., Omaha Douglas, Omaha O St., Springfield and Valley. The following Qwest wire centers in Iowa are within the Omaha MSA: Council Bluffs Manawa, Council Bluffs Downtown, Crescent, Glenwood-Mineola, Malvern, Missouri Valley, Neola and Underwood. All Qwest retail and wholesale data presented in this document relate only to these specific Qwest wire centers.

Qwest Lines Service ⁴	Retail in	December 2000	February 2004	Difference	% Change
Residence					
Business					
Total					

While various factors have contributed to these trends, including the general economic malaise and some displacement of non-primary lines by DSL service, it is indisputable that Qwest's access line base has declined dramatically and that the bulk of this decline is driven by the increase in the number of competitive alternatives to Qwest service. These alternatives include CLEC options as well as the availability of wireless and VoIP services, which are discussed in the following sections.

3. CLEC Competitive Trends

A wide range of CLECs are now competing with Qwest in the local exchange market in the Omaha MSA, and contrary to the popular belief that the CLEC industry has undergone a "meltdown" over the last two years, the aggregate number of lines served by CLECs in Qwest wire centers in that MSA has continued to grow. A number of facilities-based CLECs including Cox Communications, McLeod, Alltel and Huntel are currently providing local exchange services within Qwest's service territory in the Omaha MSA. Additional CLECs are now competing with Qwest in the Omaha MSA via resale

⁴ Excludes Public Coin and Qwest Official Company Service (OCS) access lines.

of Qwest's retail services or by the use of wholesale network elements purchased from Qwest.

The following table summarizes the change in volume in various categories of wholesale services purchased by CLECs operating in the Omaha MSA from Qwest between December 2000 and February 2004, the same time horizon shown earlier regarding the change in Qwest's retail access line base:

Qwest Wholesale Service	December 2000	February 2004	Difference	% Change
UNE Loops	Data Redacted	Data Redacted	Data Redacted	Data Redacted
UNE-Platform	Data Redacted	Data Redacted	Data Redacted	Data Redacted
UNE-Platform Directory Listings				
Residence	n/a	Data Redacted	n/a	n/a
Business	n/a	Data Redacted	n/a	n/a
Resold Lines				
Residence	Data Redacted	Data Redacted	Data Redacted	Data Redacted
Business	Data Redacted	Data Redacted	Data Redacted	Data Redacted
Local Interconnection Service (LIS) Trunks	Data Redacted	Data Redacted	Data Redacted	Data Redacted

The UNE loop data above shows that the number of lines being served by CLECs using their own switches in combination with network facilities purchased from Qwest to deliver service to the end user has more than doubled. It is important to note that the quantity of UNE loops in service does not capture any data for end users served by CLECs using CLEC-owned switches coupled to CLEC-owned loops. For example, neither end user lines served by cable telephony providers such as Cox nor end user lines

served by CLECs utilizing their own fiber networks to deliver local service to business customers are reflected in these totals.

Local Interconnection Service (LIS) trunks are network facilities that enable the exchange of traffic between Qwest and CLEC switches. As the number of end user lines served by facilities-based CLECs increases, the number of LIS trunks in service must be increased to minimize blockage of calls from CLEC customers to customers served by Qwest. LIS trunks are used by CLECs using their own loop network facilities (including coaxial loops used by cable telephone providers such as Cox) as well as those that use unbundled loops purchased from Qwest and are therefore a good barometer of the growth in the overall customer access line base served by facilities-based CLECs. It is noteworthy that the number of LIS trunks used by facilities-based CLECs has nearly doubled since December 2000 as these CLECs resized their networks to accommodate their rapidly growing customer base.

Since resale of Qwest's existing retail services represents a non-capital intensive means for CLECs to enter the market and build a core customer base, albeit with profit margin potential lower than that available via delivery of service via CLEC-owned facilities or wholesale network facilities leased from Qwest, it is not surprising that CLECs have largely moved away from resale toward other forms of local exchange service delivery. The trend in the Omaha MSA is consistent with national trends as CLECs seek greater efficiencies and margins. However, especially for new market entrants, resale remains a viable option as a means to quickly and with little investment enter any portion of the

Omaha-Council Bluffs market to attract a customer base of sufficient size to justify further investment in CLEC-owned switches and facilities.

The Unbundled Network Element-Platform (UNE-P) product has been actively used by CLECs since 2000, and the use of this service continues to increase. This service was originally used by a limited number of CLECs in Iowa, including McLeod, but has now been embraced by a greater number of CLECs, including AT&T, MCI, Sprint, Z-Tel and others as a means of delivering service to residential and small business customers, and these carriers are all now actively promoting UNE-P based services. In addition, the quantity of residential and business directory listings in the Qwest listings database associated with UNE-P lines in service in February 2004 is shown in the table. While the number of directory listings will never precisely match the number of lines in service, since some telephone numbers do not appear in the directory while others have multiple directory listings, it is noteworthy that the number of UNE-P residential directory listings is substantially greater than UNE-P business directory listings in the Omaha MSA, showing that CLECs view this wholesale service platform to be a viable means of delivering competitive local exchange service to residential customers.

Clearly, multiple CLECs have chosen to enter the local exchange market in the Omaha MSA and have done so via diverse entry strategies. The local market in this MSA is indisputably open and Qwest is no longer the dominant carrier in this market. One measure of competition in a market, albeit not the only measure, is competitor market share. While developing a precise calculation of overall CLEC market share within

Qwest service territory is difficult, as Qwest does not have access to proprietary customer information held strictly by the CLECs, an estimate can be developed using E911 residential and business customer record data reported by CLECs to Intrado, the independent E911 database administrator. The number of E911 records are not directly equivalent to the number of access lines in service, since some CLECs report Direct Inward Dial (DID) telephone numbers to Intrado (more than one DID telephone number can be associated with a single PBX trunk) and other CLECs do not report telephone numbers associated with inbound-only access lines that are incapable of originating a call to E911. However, the E911 records as a directional surrogate for the number of access lines served by facilities-based CLECs.⁵ As of April 2004, facilities-based CLECs reported to Intrado a total of **[Data Redacted]** residential E911 records and **[Data Redacted]** business E911 records in the communities in the Omaha MSA.⁶ These data can be combined with the CLEC resale and UNE-P values shown in the table above, coupled with Qwest retail access line data, to develop market share estimates for residential and business local exchange services in the Omaha MSA, as shown below:

⁵ E911 records associated with CLEC customers served via UNE-P or resale are reported to Intrado as Qwest records. Customer records in the Intrado database identified as CLEC records are only associated with CLECs utilizing their own local switches coupled with UNE loops or CLEC-owned loops to deliver local exchange service.

⁶ The Nebraska communities identified in the Intrado report in the Omaha MSA include Bellevue, Bennington, Boystown, Elkhorn, Gretna, La Vista, Offutt, Omaha, Papillion, Ralston, Springfield, Valley, Washington and Waterloo. The Iowa communities in the Intrado report include Council Bluffs, Crescent, Glenwood, Malvern, Mineola, Missouri Valley, Neola and Underwood.

	Residence	Business	Total
Resold lines	Data Redacted	Data Redacted	Data Redacted
UNE-P listings	Data Redacted	Data Redacted	Data Redacted
E911 records	Data Redacted	Data Redacted	Data Redacted
Total CLEC lines	Data Redacted	Data Redacted	Data Redacted
Qwest retail lines	Data Redacted	Data Redacted	Data Redacted
Total Omaha MSA market lines	Data Redacted	Data Redacted	Data Redacted
% CLEC lines in Omaha MSA	Data Redacted	Data Redacted	Data Redacted

In Table 6 of the FCC's Local Telephone Competition Report, released December 22, 2003, the FCC reported an overall CLEC market share in Nebraska of 20%⁷ based on a data vintage of June 30, 2003. However, these data are statewide totals and include counts in Independent Telephone Company operating territory, and carriers with 10,000 or fewer access lines were not required to report. These data also represent a timeframe over 8 months prior to the February and April 2004 data reported above, and the Omaha MSA is much more intensively competitive than the remainder of Nebraska, since Cox (Qwest's most aggressive competitor in the Omaha MSA) is not offering service in other parts of Qwest's service territory in the state. When these factors are considered, the FCC's own data shows that the CLEC share estimate shown above is realistic and likely understated.

⁷ The statewide 20% CLEC market share shown in the FCC's report for Nebraska ranks as fifth highest in the country, trailing only New York, Rhode Island, Michigan and Kansas.

It is also important to note that these "share" estimates do not contemplate intermodal telephone service substitutes, such as wireless and VoIP services, now available to customers within Qwest's service territory in the Omaha MSA. These intermodal service alternatives are discussed in following sections.

All local service providers report information to Telcordia regarding the configuration of their networks established to provide local exchange services. This information is contained in the Local Exchange Routing Guide (LERG). For example, incumbent LECs, CLECs and wireless providers all report local switches deployed in each state, the area codes and prefixes assigned to each switch, the rate centers served by those switches, type of switches deployed and the physical location of those switches. This information is used by the industry to program all switches to ensure calls to each prefix can be processed. The LERG shows a total of eight CLECs with prefixes assigned to switches serving rate centers in the Omaha-Council Bluffs MSA. In several instances, the CLEC declined to specify the type of switch used and notes simply a switch type of "digital switching system." However, the LERG shows that one DMS 500, one DMS 100/200 and one 5ESS switch are located in Omaha to serve this market. A DMS 500 and DMS 100/200 can each serve a maximum of 100,000 access lines, while a 5ESS can serve 200,000 access lines. In other words, these three Omaha CLEC switches alone can accommodate approximately 400,000 end user lines, which is nearly double the number of facilities-based CLEC lines in currently in service in the Omaha MSA. The unidentified switches of the other Omaha CLECs are in addition to that capacity.

Clearly, there is ample capacity in CLEC switches now deployed to serve the Omaha MSA to absorb significant additional line growth.

While Qwest is experiencing competitive pressure from a number of CLECs in the Omaha MSA, Cox, McLeodUSA and Alltel are currently the most significant in this geographic area. The following sections describe the scope of these competitors' operations, with particular emphasis on Cox, which has succeeded in deeply penetrating the local exchange market in the Omaha MSA.

Cox

In February 2004, Cox Communications announced it is now serving one million digital telephone subscribers nationwide: "Cox's successful seven-year history of providing primary line telephone service is key to its bundling strategy and has resulted in more than one million telephone customers. In Cox's most mature markets, one in three homes subscribe to Cox Digital Telephone."⁸ In reporting fourth quarter and full year financial results for 2003, Cox stated:

We grew our Cox Digital Telephone customer base by 38 percent in 2003, with a record number of new phone subscribers added in the fourth quarter. Cox's telephone service is now available to 48 percent of our homes passed, and we will use VoIP technology and our IP backbone to further expand our footprint during 2004.⁹

⁸ *Cox Communications Surpasses Five Million Digital Service Subscriptions*, February 12, 2004, www.cox.com, visited February 27, 2004. Since Cox began offering telephone service in Omaha in 1998, it can reasonably be concluded that Omaha falls within this category.

⁹ *Cox Communications Announces Fourth Quarter and Full-Year Financial Results for 2003*, www.cox.com, visited February 27, 2004.

According to Cox's website, the company offers Digital Telephone Service in the following exchanges in Nebraska and Iowa: Bennington, Elkhorn, Gretna, Omaha, Valley, Waterloo, Carter Lake, Council Bluffs, and Crescent.¹⁰ Attachment 1 to this Exhibit is a page from Cox's website which describes the local calling areas for each of these exchanges.

In an investor meeting held on May 9, 2002, Cox described its Omaha operation, stating its mission for the area is "to be the premier provider of voice, video and data in the markets we serve ... while operating in a head-to-head competitive environment." Cox stated that as of April 30, 2002, the Omaha system was comprised of 295,863 serviceable homes, 360,000 total residential RGUs,¹¹ and 7,587 commercial customers. At that time—two years ago - Cox estimated its residential telephony market share to be 26.5%. At the conference, Cox reported that residential telephony penetration was approaching 50% of its basic cable customer base in Omaha.

Cox also informed the investor community that its retail stores generate 15% of connects, with 5% of connects coming through its partnership with Buffet-owned Nebraska Furniture Mart. At that time (May 2002), Cox indicated it had 25 retail outlets in the Omaha area. Cox has experienced a consistent growth rate of one percent per month in its product bundles, with 44% of its customers owning a bundle of services.¹² The company found that customers with three-product bundles are five times less likely to

¹⁰ www.cox.com/Omaha/telephone/localareas.asp, visited April 16, 2004.

¹¹ A Cox acronym representing Revenue Generating Units, which are essentially households that are potential or current Cox customers within the defined market.

¹² Cox Communications Omaha Investor Meeting, May 9, 2002.

leave than others.¹³ Omaha customers who subscribe to a three-product bundle consisting of Cox Digital Telephone, Cox High-Speed Data and Cox Cable TV receive discounts off the standard individual rate. Customers may choose to receive \$10 off their entire bill or one free primary access line of Cox Digital Service.¹⁴

Cox entered the business telephony market in Omaha in June 1998, primarily focusing on small-to-medium businesses.¹⁵ Cox's strategic objective is to "own the business customer relationship for all services Voice-Video-Data."¹⁶ As of year-end 2002, Cox Business Services was realizing almost \$1.2M per month in revenue, from almost 16,000 business customers. Sixty-eight percent of its revenue was from switched telephone, three percent from unswitched telephone, 27% from data, and two percent from "other."¹⁷

Cox also described its Omaha network for investors as having the following attributes:

- 4,000 Network Miles
- Fully certified for Video, Telephone and High Speed Data
- One Master Telecommunications Center and 6 Secondary Centers (in North Omaha, Council Bluffs, South Omaha, Bellevue, West Omaha, and Elkhorn)
- High Reliability

¹³ *Id.*

¹⁴ Nebraska PSC Tariff No. 1, Page No. 108, Effective October 6, 2000.

¹⁵ *Id.*

¹⁶ *Id.*

¹⁷ *Id.*

Cox concluded its presentation to investors by affirming that it is "positioned to take advantage of new services, and for continued growth." Cox's stated "continued growth" objective is affirmed in its Form 8-K SEC filing submitted on April 29, 2004. In that filing, Cox reported it "added 78,959 Cox Digital Telephone customers, ending the quarter with 1.1 million telephone customers, representing year-over-year customer growth of 36%." While these data represent results from Cox's operations across the country, they suggest that Cox is adding telephone subscribers at a very robust pace, in marked contrast to subscriber access line trends of the incumbent LECs.

Cox offers a wide range of services to residential and business customers. In addition to stand-alone access lines, Cox offers residential customers a variety of popular calling features including Voice Mail, Call Forwarding, and 3-Way Calling, just to name a few. For Cox customers purchasing another Cox service, residence access lines are available for \$15.89 per month in Nebraska and \$11.39 per month in Iowa. Second lines are available for \$7.89 per month in Nebraska and \$6.50 per month in Iowa.¹⁸ Prices for non-Cox residential customers are \$17.65 per month for the first line and \$16.35 per month for the second line in Nebraska and \$12.65 per month for each line in Iowa.¹⁹ Installation of phone jacks and inside wiring is also available from Cox.²⁰ In addition, wire maintenance plans are available, as are packages such as the Connection 60 Package (consisting of one phone line, the Solutions feature package and long distance for \$29.95 per month) and the Connection Unlimited Package. Priced at \$49.95 per month, this

¹⁸ www.cox.com/Omaha/telephone/Pricing.asp, visited April 16, 2004.

¹⁹ *Id.*

²⁰ https://orders.cox.com/DigitalTelephone/feature_selection.asp, visited April 16, 2004. Inside wire and jacks may also be installed by the building owner, by an electrician, or by an independent contractor.

package includes the phone line, the Control Plus feature package, Voice Mail, and unlimited long distance calling within the United States.²¹ Features are available on a stand-alone basis, without the requirement to purchase a package of services, if that is the customer's preference.²²

Cox's Local Exchange Service includes Basic Residential Service, Basic Business Service, PBX Service (trunks), Centrex Service, ISDN-PRI, and Message Telecommunications Service.²³ Other services available from Cox include Directory Assistance, Operator Assistance, Directory Listings, Emergency Services, Vanity Telephone Numbers, and miscellaneous services such as Toll Restriction, Temporary Suspension of Service – Customer Initiated, and Number Referral Service. Cox also has tariffs on file with state commissions for Switched Access and Dedicated Transport (Nebraska PSC Tariff No. 2 and Iowa Tariff No. 2).

Attachment 2 to this Exhibit provides maps depicting the geographic coverage of Cox's footprint in the Omaha/Council Bluffs area. The maps were developed by Qwest and are based on publicly available information regarding telephone service availability from the Cox web site. The area bordered by the gold line represents the boundary of the Omaha MSA, which contains territory served by Qwest (primarily the greater Omaha and Council Bluffs areas) as well as areas served by Independent Telephone Companies. The areas shaded in red, which overlay Qwest's service territory in the Omaha-Council Bluffs

²¹ www.cox.com, visited April 16, 2004.

²² www.cox.com/Omaha/telephone/pricing.asp, visited April 16, 2004.

²³ Nebraska PSC Tariff No. 1, Iowa Tariff No. 1.

MSA, are areas in which Cox offers the "triple play" - cable television, cable modem and telephone service.

Late last year, Cox announced it is experiencing record growth in revenue and customer locations in the business market through its commercial broadband division.²⁴ "Cox is in a unique position in the commercial services arena," said Bill Stemper, vice president of Cox Business Services in Atlanta. "All of our pieces --- from the network we own and manage, to our architecture with built-in reliability to the business solutions and expertise we offer to small- and medium-sized business owners and enterprise alike --- contribute to the sense of trust that our customers have with us."²⁵

Cox has great breadth in its customer base, which encompasses residential subscribers, enterprises, small and medium businesses as well as government properties and teleworkers/home offices. Many school systems and air force bases, hospitals, enterprise and airports, law firms and teleworkers trust Cox for the delivery of circuit-switched telephone and long distance services, high-speed Internet access, web hosting, VPN and data transport services. Approximately 40 percent of Cox's commercial services customers choose to bundle their voice and data services, according to company research.²⁶

²⁴ A Cox customer location is a single business location with one or more active Cox data, voice or transport services on one or more accounts. Video-only business customers are not included in these figures.

²⁵ www.coxbusiness.com/PR/03-1027.html, visited March 1, 2004.

²⁶ *Id.*

Attachment 3 to this Exhibit contains advertisements in which Cox promises businesses they can save up to 20% by subscribing to Cox communications packages. Business local lines are available for \$26.89 per line per month in Omaha and \$28.50 in Council Bluffs and other Iowa communities served by Cox. Trunks are offered for \$37.50 per month in Omaha and \$28.50 in Iowa. Term discounts are available. The Cox Office Solutions Pak ("COSP") offers business customers in Omaha a bundled package term plan of one or three-year commitments. The package combines telephony services, including two flat-rated business access lines, eight custom calling features, a block of 200 minutes of interstate and intrastate long distance calls, with Cox's high-speed Internet access service. The total package is priced at \$88.10 per month with a one-year contract or \$76.74 per month for a three-year contract. Customers who enter into the three year contract do not pay installation charges which amount to \$250 with a one-year contract.²⁷ Additional packaged offerings are available to Cox business customers.

Cox regularly makes promotional offerings available to Omaha-area consumers. For example, Cox has offered free activation to residential customers who subscribe to Cox Digital Telephone Service via the company's website²⁸, three months free service to new residential customers²⁹, up to three months free service plus free features and free installation to business customers who switch to Cox³⁰, and a \$100 gift card to current

²⁷ Nebraska PSC Tariff No. 1, Pages 109 and 110, Effective March 24, 2003.

²⁸ Free Activation with Online Ordering, Nebraska PSC Tariff No. 1, Page No. 102.1, Effective August 18, 2003.

²⁹ Three Months Free MRC, Cox Nebraska PSC Tariff No. 1, Page No. 102.2, Effective September 1, 2003.

³⁰ www.coxbusiness.com/systems/ne_omaha/Jan_04/index_omaha.html, visited April 16, 2004.

Cox Business customers for referrals resulting in a sale³¹. These are just a few of the numerous incentives Cox offers to current and prospective customers.

Another example of the flexibility Cox enjoys in the marketplace is evident in Cox's Iowa Tariff No. 1. That tariff indicates Line Connection Charges may be waived *in competitive situations* (emphasis added).³² According to Cox's tariff on file with the Iowa Board, the normal line connection charge is \$40.00 for Business customers and \$29.95 for Residence customers.³³

Cox regularly positions its services as having greater value than the services provided by Qwest. For example, on its website, Cox compares the price of Cox's lines and features to those offered by Qwest, and calculates the "percent savings" for consumers who sign up with Cox. A sample is included as Attachment 4 to this Exhibit. Cox has been aggressive in promoting its services via door hangers in the Omaha area, especially in areas where Qwest is deploying DSL capability. For example, Qwest was provided a Cox door hanger that was left at the front door of an Omaha resident on April 20, 2004 promoting a bundled Cox service offering consisting of cable television service priced at \$19.08, high speed internet service priced at \$19.99 and telephone service priced at \$2.25 (the low telephone service price is only available if purchased as part of the bundle of Cox services).

³¹ www.coxbusiness.com/referabiz, visited April 16, 2004.

³² Iowa Tariff No. 1, Page No. 64, Effective September 28, 2003.

³³ *Id.*

McLeodUSA

McLeodUSA's fiber optic network spans 25 states, providing local, long distance, wireless, data and Internet service to rural and metropolitan areas. The company owns, operates, and maintains a full range of facilities on a national basis, including 44 voice switches.³⁴ In February, 2004, McLeodUSA reported year-end 2003 results, including the following customer platform statistics:³⁵

<u>2003</u>	<u>2002</u>
* 65% - UNE-L ³⁶	* 52% - UNE-L
* 5% - Resale	* 15% - Resale
* 30% - UNE-M/P	* 33% - UNE-M/P

McLeodUSA also reported a reduction in revenue from the previous year, "primarily driven by the FCC mandated reduction in access billing rates and a lower customer base, of which approximately 28,000 customers valued at \$9.5 million of revenue resulted from the Company's intentional drive to eliminate non-profitable customers."³⁷ It's apparent that McLeodUSA is not subject to Provider of Last Resort requirements such as those imposed upon Qwest and is able to selectively choose the customers it serves.

On January 21, 2004, McLeodUSA announced plans to deploy the next generation of Preferred Advantage services utilizing Internet Protocol (IP) technology. The new

³⁴ www.mcleodusa.com, visited March 1, 2004.

³⁵ *McLeodUSA Reports Fourth Quarter and Total Year 2003 Results*, February 18, 2004.

³⁶ These lines are provisioned through McLeod switches.

³⁷ *McLeodUSA Reports Fourth Quarter and Total Year 2003 Results*, February 18, 2004.

Voice-over-IP ("VoIP") platform will be launched early in the second quarter across the McLeodUSA network to initially offer McLeodUSA business customers an enhanced set of flexible features for their local, long distance and Internet services via McLeodUSA's highly successful Integrated Access product. McLeodUSA will also utilize VoIP to lower cost and enhance other Preferred Advantage services for both residential and business customers in the near future.³⁸

McLeodUSA has been named the primary local telecommunications provider for 538 Walgreens stores with nearly 5,000 business lines in its 25-state footprint.³⁹ K-Mart has also chosen McLeodUSA to provide local telephone services to 176 locations, including two distribution centers, in fourteen Midwestern and Western states.⁴⁰ Section 5 of McLeodUSA's Nebraska Tariff No. 3 and Iowa Utilities Board No. 4 lists the cities and wire centers where McLeod is offering service, either over its own switch or through the use of network elements. The Tariffs demonstrate McLeodUSA is offering residential and business service in the Omaha MSA.

McLeodUSA offers residence and business customers stand-alone as well as bundled offerings. The rate for a stand-alone residential access line in Council Bluffs is \$21.95

³⁸ *McLeodUSA Reports Fourth Quarter and Total Year 2003 Results*, February 18, 2004.

³⁹ *McLeodUSA Selected as Primary Local Telecommunications Services Provider by Walgreens*, April 28, 2003;

⁴⁰ *McLeodUSA Selected as Primary Local Telecommunications Services Provider by Kmart*, August 11, 2003.

per month. In Omaha, the monthly rate is \$23.95. The rate for a stand-alone business access line in Omaha and Council Bluffs is \$31.95 per month.⁴¹

In late 2002, McLeodUSA launched its Preferred Advantagesm portfolio of residential bundled packages in Iowa and Nebraska.⁴² The "Value Preferred Package" for residence customers, consisting of local line switched service, Call Waiting, Three Way Calling, Call Forward Variable, Caller ID, Anonymous Call Rejection, Call Waiting ID, 900 Blocking, and a primary directly listing, is available for \$34.95 per month in Omaha and \$36.95 in Council Bluffs. The "Premium Preferred Package," including residential local switched service, Call Waiting, Three Way Calling, Call Forward Variable, Caller ID, Anonymous Call Rejection, Call Waiting ID, 900 Blocking, Last Call Return, Continuous Redial, Call Screening, Speed Call 8, and a primary directory listing, is priced at \$37.95 per month in Council Bluffs and \$38.95 in Omaha.⁴³

In July 2003, McLeodUSA launched its Preferred Advantagesm integrated access service platform geared toward small and medium-sized business customers with 6 – 20 voice lines. The product allows businesses to combine local, long distance and Internet services over a dedicated, digital facility.⁴⁴ The "Simple Preferred Package" for Small Businesses consists of a local switched line and three features for \$31.95 per month in

⁴¹ Tariff Iowa No. 4, Sheet No. 66, Effective February 18, 2004, Sheet No. 68, Effective February 18, 2004; Tariff Nebraska No. 3, Sheet No. 101, Effective January 30, 2004, Sheet No. 98, Effective January 30, 2004.

⁴² *McLeodUSA Expands Residential Communications Services Into Eight Additional States*, April 2, 2003.

⁴³ Tariff Nebraska No. 3, Sheet No. 101, Effective January 30, 2004, Tariff Iowa No. 4, Sheet No. 68, Effective February 18, 2004.

⁴⁴ *McLeodUSA Launches Preferred Advantagesm Integrated Access Service Platform*, July 22, 2003.

Omaha and Council Bluffs.⁴⁵ Additional packages are available at incrementally higher rates, based on the number of features included in the package. In addition to the above-referenced services, McLeodUSA offers Intercept Services, Local T1 Service, Dynamic T-1 Service, PRI ISDN, Directory Service, Conference Calling Service, Directory Assistance, Operator Services, Long Distance and 800 Services, Market Expansion Line, and Private Switch Automatic Location Identification. Furthermore, McLeodUSA offers trouble isolation and inside wire care plans to its customers.

Promotional offerings and term and volume discounts are also available.⁴⁶

McLeodUSA's Nebraska tariff detailing its flexibility to promote reads as follows:

McLeodUSA may from time to time engage in special promotions of limited duration. These promotions may be in the form of waiver or reduced recurring and nonrecurring fees, lowered usage charges, or other actions designed to attract new customers or to increase existing customer awareness of a particular service. All promotions will be offered on a non-discriminatory basis to eligible customers.⁴⁷

Alltel

Alltel Communications of the Midwest ("Alltel") was certified by the Nebraska PSC on March 10, 1997⁴⁸ as a CLEC and has the authority to offer local service anywhere in the state. Alltel is a full service provider, offering residential and business local exchange service, DSL, long distance and wireless services to customers in the Omaha area. In the

⁴⁵ Tariff Nebraska No. 3, Sheet No. 98, Effective January 30, 2004; Iowa Tariff No. 4, Sheet No. 86, Effective February 18, 2004.

⁴⁶ Tariff Nebraska No. 3, Iowa Tariff No. 4.

⁴⁷ Tariff Nebraska No. 3, Sheet No. 60, Effective March 28, 2004.

⁴⁸ Application No. C-2544.

Commission's Annual Report to the Legislature on the Status of the Nebraska Telecommunications Industry, released in September 2003, Alltel is reported as the second largest local exchange carrier in the state with a total of 274,416 access lines (24.7% of the access lines in the state) as of February 2003. Far from being a relatively small Independent, it has significant operational scale and scope, and Alltel reports in its web site that it is:

"a customer focused communications company with almost 13 million customers and \$8 billion in annual revenues. Alltel provides wireless, local telephone, long distance, Internet and high-speed data services to residential and business customers in 26 states."⁴⁹

Alltel has operated traditionally as an Independent LEC in Nebraska, but reported to the PSC for the annual report that it now serves 3,152 residential and 19,184 business lines as a CLEC in the state, primarily in Qwest's service territory in the greater Omaha area.

Alltel offers ala carte services, but also emphasizes service bundles to Nebraska customers as is typical of service offerings of Qwest and CLECs serving the state. In fact, Alltel offers a total of six primary packages, including the Caller ID Package, the Complete Package, Basic Connections, Preferred Connections, Web Connections and DSL Connections⁵⁰ which are built upon Alltel's ability to integrate local service, long distance, calling features and internet access for its customers. Integration of this sort is widely recognized in the telecommunications industry as being a key to meeting customer demands and thereby enhancing the provider's opportunity for market success.

⁴⁹

http://www.alltel.com/news_information/newscenter.html, visited May 24, 2004.

⁵⁰

www.alltel.com/estore/local/alltelbundles/index.html, visited May 24, 2004.

4. Wireless Service

In its most recent Local Telephone Competition report, the FCC showed a total of 900,744 wireless subscribers in Nebraska as of June 2003.⁵¹ In the same report, the FCC showed a total of 775,829 ILEC (Qwest and Independents combined) access lines in service for the same month. In other words, the number of wireless subscribers now exceeds the total number of ILEC switched access lines in service in the state. Wireless phones are now widely accepted by business and residential consumers for voice telephony. In addition, wireless providers are now augmenting their services with data applications such as dial-up wireless internet access, text messaging and image transmission to bring additional functionality to their services to attract and retain customers. Clearly, a segment of the Qwest customer base views wireless service as an acceptable alternative to primary or additional wireline access lines, and this segment has contributed to the decline in Qwest's retail access line base.

A wide range of wireless providers is now offering service within Qwest territory in Nebraska, including such significant carriers as Verizon, Sprint, AllTel, Cricket, Nextel, U.S. Cellular and MCI. Service is available from at least one of these carriers in every Qwest wire center in the Omaha MSA. Each of these carriers has significant scale and scope and is actively promoting the availability of its service to customers in the state.

On November 24, 2003, wireless number portability was implemented in response to an FCC mandate. Wireless number portability will not only enable wireless subscribers to

⁵¹ FCC Local Telephone Competition Report, Table 13, December 22, 2003.

retain a preexisting wireless telephone number when changing wireless service providers, it will also enable customers to retain a preexisting wireline telephone number when the customer elects to disconnect the wireline service entirely and rely solely on wireless service as the customer's primary telecommunications service. This event removes a barrier that may have prevented some wireline customers from "cutting the cord" and substituting wireless service for traditional Qwest wireline telephone service. Research released in January 2004 by Advantis⁵² assessed the impact of wireless number portability on the proportion of residential wireline customers willing to completely substitute wireless service for traditional wireline local exchange service. Advantis found that, assuming availability of a wireless plan priced at \$40/month and containing 600 plan minutes, 6.4% of the respondents reported a willingness to completely substitute wireless for wireline service without number portability. When the respondent was informed of the availability of wireless number portability, the percentage of respondents willing to "cut the cord" increased to 11.5%. On a nationwide basis, Advantis projects that wireless service will erode the wireline telephone base at an increasing rate and predicts that 6 million wireline telephone lines will be displaced by 2007 and 14 million by 2009.

Wireless companies offer a variety of plans - local plans, regional plans, and national plans - with varying amounts of minutes included. Generally, wireless packages including long distance and features start as low as \$20.00 per month. As a point of comparison, consider that in Nebraska Qwest's flat-rated local exchange residence line is priced at \$23.22 (\$18.15 basic rate within the base rate area plus \$5.07 Subscriber Line

⁵² Mobile Metrics: Wireline to Wireless Displacement Study (Advantis: January 2004). This research was a telephone survey of 1,000 residential households in the top 100 MSAs and was conducted in November and December 2003.

Charge), excluding any charges for features or intraLATA long distance. The comparable Qwest business rate is \$32.62 (\$27.55 within the base rate area plus the \$5.07 Subscriber Line Charge). Verizon offers customers within its service territory in Nebraska (including the Omaha MSA) a \$34.99 per month plan which includes 400 "whenever" minutes, unlimited weekend minutes, VoiceMail, Caller ID, Call Waiting, Call Hold, and nationwide long distance.⁵³ Cricket offers unlimited local calls to Omaha consumers for \$35.99 per month, including VoiceMail, Caller ID, Call Waiting and Three-Way Calling features.⁵⁴ Alltel offers the "Local Freedom" plan in the Omaha MSA for \$39.95 per month, which includes 700 "anytime" minutes, unlimited night/weekend calling, VoiceMail, Caller ID, Call Waiting and Three Way Calling.⁵⁵ Sprint offers a "Free and Clear" plan that includes 300 anytime minutes, unlimited night and weekend minutes, nationwide long distance, voice mail, Three-Way Calling, Caller ID and Three Way Calling for \$35.00per month.⁵⁶ These examples represent only a very small number of the wireless plans and services that are available to consumers and businesses in the Omaha MSA. For small business and residence customers that that have communications needs that can be satisfied by the service attributes offered by the wireless carriers, a few of which are shown in the above examples, wireless service is clearly an attractive alternative to Qwest's wireline service.

⁵³ www.verizonwireless.com visited 4/20/04.

⁵⁴ www.cricketcommunications.com, visited 4/21/04.

⁵⁵ www.alltel.com, visited 4/21/04.

⁵⁶ www.nextel.com, visited 5-4-04.

5. Voice over Internet Protocol (VoIP) Telephony

Voice over Internet Protocol (VoIP) service is quickly evolving as a direct substitute for Qwest wireline telephone service, and the service functions in a manner very similar to standard telephone service familiar to Qwest's customers. For example, the VoIP customer utilizes a standard telephone set to originate and receive telephone calls, and the dialing patterns are identical to standard wireline telephone service. The customer's telephone set is simply plugged into an interface device that enables the telephone call to be processed over a broadband connection via the Internet. Currently, VoIP providers do not pay Switched Access charges for origination of this type of traffic, enabling VoIP providers to offer very low long distance rates.⁵⁷ For example, Vonage offers free long distance within the continental United States and Canada, and international long distance rates from the U.S. are priced as low as \$0.02 per minute. Typically, long distance carriers charge \$0.30 per minute or more for the same call.

Qwest is aware of at least seven vendors now offering VoIP telephony applications to consumers in Nebraska. AT&T offers a "suite" of VoIP products for business customers and is in the process of rolling out its residential service entitled "CallVantage." While not yet available in Nebraska, the company plans to offer CallVantage in 100 major markets by the end of 2004.⁵⁸ Five Star Telecom is also a provider of VoIP products and services, offering service under the "earthphone" trade name. In addition, Vonage,

⁵⁷ Qwest recently announced it is eliminating connection fees carriers pay when their customers make Internet-based phone calls to Qwest local-telephone customers in a move to promote true VoIP services.

⁵⁸ *AT&T will offer Internet phone calls in selected markets*, Wall Street Journal, March 31, 2004.

Packet8, VoicePulse,⁵⁹ BroadVoice, and Zipglobal offer telephony services utilizing VoIP technology.

VoIP services are priced competitively with Qwest wireline services, especially for customers with existing broadband internet access. Vonage offers a "Residential Premium Unlimited Plan" priced at \$30.00⁶⁰ per month that includes unlimited local and long distance calling within the U.S. and Canada, free Call Waiting, Voice Mail, Call Forwarding, Repeat Dialing, Call Transfer, Caller ID, and Three-Way Calling. Alternatively, residential customers may subscribe to Vonage's "Unlimited Local/Regional Plus Plan" and receive unlimited local and regional service plus 500 nationwide and Canada long distance minutes, as well as all of the features included in the Premium Unlimited Plan for \$24.99 per month. Vonage's "Small Business Unlimited" plan, priced at \$49.99 per month, provides unlimited local and long distance calling within the U.S., as well as a free fax line, free Call Waiting, Voice Mail, Call Forwarding, Repeat Dialing, Call Transfer, and Caller ID Blocking. The "Small Business Basic Plan" provides all the same free features as the Small Business Unlimited Plan, with 1500 local and long distance minutes for \$39.99 per month. In addition, Vonage allows its customers to select the area code they would like assigned to them. For example, a Vonage customer doing significant business volumes with Los Angeles customers may elect a Los Angeles area code. By so doing, all calls from Los Angeles

⁵⁹ VoicePulse service is available anywhere in the country where broadband Internet access is available, however, it is currently not offering numbers within Nebraska area codes.

⁶⁰ Vonage announced on May 17, 2004 that it was reducing its unlimited calling plan from \$35.00 to \$30.00. Vonage CEO Jeffrey Citron stated that the reduction was due to the company hitting and "inflection point, where its growing base of users had allowed it to lower costs and pass along some savings to customers." *Internet Phone Service Vonage Hits 155,000 Users*, Reuters, May 17, 2004.

customers to the Vonage customer are toll-free. Consumers subscribing to Vonage's service may also elect to keep their current phone number.

Another example of a VoIP service provider is Packet8. This VoIP provider offers its "Freedom Unlimited" residential plan for \$19.95 per month. This plan provides several features and unlimited calling to anyone in the 50 states and Canada and Packet8 subscribers worldwide. Packet8's "Virtual Office" plan, priced at \$39.95 per month, also includes business class voice mail, an auto-attendant to answer calls, conference call bridge service, hold music, three-digit dialing, as well as unlimited calling plans to the United States and Canada. Similar to the Vonage offering, Packet8 allows the customer to select the geographic "rate center," which allows incoming calls from customers in that geographic area to call the Packet8 customer toll-free. Calls between Packet8 customers anywhere in the world are always free.

As stated previously, Qwest's stand-alone basic exchange rate, excluding features and long distance, is \$23.22 for residence and \$32.62 for business. For Qwest's residential and business customers with access to a broadband Internet connection and who use calling features and make long distance calls, these services represent a viable and price-competitive alternative to traditional local exchange service.

It is clear that the competitive paradigm is changing in the local exchange market. Recently, there have been a number of public announcements regarding VoIP deployments demonstrating that carriers are now very serious about utilizing this

alternative technology to capture and retain customers. Qwest became the first regional Bell operating company to offer residential telephone service using VoIP technology, with a roll-out of the service in Minnesota in early December 2003. Also, within the past several months carriers such as Verizon Communications, SBC, BellSouth, and Time Warner announced plans to begin offering or broaden existing VoIP offerings. Vonage announced that it has struck an agreement with Circuit City stores across the country to market its services.⁶¹ Packet8 just announced that it is interconnecting its VoIP network with FreeWorld Dialup, the world's leading free Internet Telephony community.⁶² This will allow subscribers to Packet8's service to call or be called by FreeWorld Dialup subscribers. "The interconnection of voice over IP networks is a trend that will continue as more and more people incorporate VoIP calling into their lives," according to Bryan R. Martin, Chairman and Chief Executive Officers of 8 x 8, Inc. "We expect to see much more activity in this area in the near-term, as VoIP telecommunication service providers like Packet8 endeavor to lower the call routing costs for their customers even further. VoIP interconnects also improve the voice quality over that possible on switched networks, so consumers will finally start to hear what they have been missing on the legacy telephone network," Mr. Martin concluded.⁶³ InfoTech, a research and consulting firm, projects that over two-thirds of U.S. Small and Mid-Sized Business Centrex users will convert to IP Telephony by the year 2008.⁶⁴

⁶¹ *Internet Phone Service Slowly Enters Mainstream*, San Jose Mercury News, April 6, 2004.

⁶² *Packet8 and FreeWorld Dialup Now Offer Free Unlimited Calling Between Subscribers*, PR Newswire, March 30, 2004.

⁶³ *Id.*

⁶⁴ *Small Businesses Set to Abandon Centrex – InfoTech Sees Broad SMB Shift to IP Telephony*, Market Wire, Incorporated, April 30, 2004.

While empirical evidence of competition for Qwest's local exchange services has in the past focused primarily on traditional wireline CLEC-based competition, the growing presence of VoIP services, as well as wireless services, is a further indication that the competitive paradigm is changing and additional local retail service options for consumers in the Omaha MSA are now available.

6. Conclusion.

The Omaha MSA is now one of the most competitive markets in Qwest's fourteen state region. Major CLECs, including Cox, Alltel and McLeod, have deeply penetrated the local exchange market in the Omaha-Council Bluffs area and have contributed directly to the reduction of over **[Data Redacted]** in Qwest's retail access line base in this MSA. Intermodal competition is also a significant factor in the Omaha MSA. There are currently at least seven wireless providers serving the Omaha-Council Bluffs market, and according the FCC's Local Competition Report, wireless subscribers now outnumber traditional landline access lines in Nebraska. With the advent of wireless number portability in November 2003, landline customers are now free to retain their preexisting telephone numbers when electing to subscribe only to cellular/PCS service for their communications needs. Number portability will accelerate the trend of displacement of landlines with cellular phones. Additionally, VoIP service is available from at least seven providers to any residential or business customer in the Omaha MSA with access to a broadband internet connection. VoIP is emerging as a viable substitute for traditional local exchange and long distance services and is being embraced by major

telecommunications providers as a core telecommunication service platform. In small business and residential applications, VoIP services can easily be self-installed by the customer in as little as ten minutes. Clearly, VoIP is a present and ever-increasing competitive factor in the local exchange market in the Omaha MSA.

The range of competitive options available to customers in the Omaha MSA has resulted in a steep erosion in Qwest's retail access line base, and Qwest is no longer the dominant carrier in this market. In view of this range of competitive alternatives, Qwest must be reclassified by the FCC as non-dominant in the Omaha MSA.